

Message Text

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ACTION TRSE-00

INFO OCT-01 EA-06 ISO-00 EB-07 SP-02 AID-05 NSC-05 RSC-01

CIEP-01 SS-15 STR-01 OMB-01 CEA-01 L-02 PA-01 PRS-01

USIA-06 H-01 CIAE-00 COME-00 FRB-01 INR-05 NSAE-00

XMB-02 OPIC-03 LAB-04 SIL-01 /073 W

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P R 030312Z DEC 74

FM AMCONSUL HONG KONG

TO SECSTATE WASHDC PRIORITY 3058

INFO AMEMBASSY MANILA

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PASS TREASURY FOR PELIKAN FROM GORDON

E.O. 11652: N/A

TAGS: EAID, EFIN, RP

SUBJECT: CONSULTATIVE GROUP MEETING FOR THE PHILIPPINES DECEMBER 9 AND

10:

COMMENTS ON THE ISSUES

1. THE ISSUES THAT MIGHT BE RAISED AT THE CONSULTATIVE GROUP MEETING WHICH HAVE THE MOST BEARING ON THE REQUIREMENTS FOR EXTERNAL ASSISTANCE CALCULATED IN THE IBRD REPORT (PHL 74-3, 11/11/74) ARE THOSE RELATED TO:

- A) THE DOMESTIC INFLATION AND ITS EFFECT ON IMPORT DEMAND AND,
- B) THE WILLINGNESS OF THE AUTHORITIES TO MAINTAIN A REALISTIC EXCHANGE RATE.

2. ONE OF THE MAJOR PROBLEMS FACING THE PHILIPPINES IN THE NEXT YEAR IS SLOWING THE RATE OF INFLATION. NOT ONLY DOES THE HIGH RATE OF PRICE RISE LEAD TO A REDISTRIBUTION OF INCOME AGAINST URBAN SALARIED EMPLOYEES BUT TO AN INTENSE DEMAND FOR IMPORTS. THE IBRD REPORT INDICATES THAT NON-OIL IMPORTS, IN CONSTANT PRICES, WILL RISE 19 PERCENT IN 1974 AS COMPARED TO A PROBABLY OPTIMISTIC LIMITED OFFICIAL USE

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ESTIMATE OF 7 PERCENT FOR GNP GROWTH.

3. BY TAKING THE 1974 ESTIMATES AS A BASE FOR ITS ESSENTIALLY REASONABLE IMPORT PROJECTION FOR FUTURE YEARS, THE REQUIREMENT FOR EXTERNAL ASSISTANCE TEND TO BE INFLATED. FOR EXAMPLE, IF NON-OIL IMPORTS HAD RISEN 8 PERCENT, IN REAL TERMS, IN 1974, AND ASSUMING THE SAME RATE OF INCREASE OF IMPORT PRICES, TOTAL FOREIGN EXCHANGE EXPENDITURES WOULD BE REDUCED \$250 MILLION IN 1974. CARRYING THAT ADJUSTMENT FORWARD FOR 1975-65 WOULD LARGELY ELIMINATE THE FUNDING SHORT FALL (IBRD REPORT, P. 42).

4. SINCE THE PHILIPPINES HAS A FAIRLY OPEN ECONOMY, IN PRACTICE, (BECAUSE SMUGGLING AND OTHER FORMS OF EVASION OFFSET CONTROLS) THE APPROPRIATENESS OF ITS EXCHANGE RATE IS ONE OF THE MAJOR DETERMINANTS OF IMPORTS. THAT RATE HAS PROBABLY BEEN QUITE REALISTIC UNTIL THIS YEAR BUT THE RECENT RISE OF PRICES MAY HAVE CHANGED THE SITUATION. BY ALLOWING THE EXCHANGE RATE TO DEPRECIATE SLOWLY IN THE PAST FEW MONTHS, THE CENTRAL BANK HAS RECOGNIZED THE NEED FOR A CORRECTION. SOME OF THE "GAP" PROJECTED FOR 1975-67 MAY REALLY BE THE EXTRAPOLATION OF THIS YEAR'S SOMEWHAT OVERVALUED EXCHANGE RATE. TO A CERTAIN EXTENT, COMMODITY LOANS AND EXCHANGE RATE ADJUSTMENTS ARE SUBSTITUTES FOR ONE ANOTHER IN THE AREAS OF IMPORT DEMAND AND THE COMPETITIVE POSITION OF MANUFACTURED EXPORTS. THE GOVERNMENT'S INTENTIONS SHOULD BE DISCREETLY PROBED.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC ASSISTANCE, INFLATION, MEETINGS, FOREIGN EXCHANGE RATES
Control Number: n/a
Copy: SINGLE
Draft Date: 03 DEC 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: izenbei0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974HONGK13036
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D740349-0855
From: HONG KONG
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19741265/aaaacdx.c.tel
Line Count: 85
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION TRSE
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 2
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: izenbei0
Review Comment: n/a
Review Content Flags:
Review Date: 24 JUL 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <24 JUL 2002 by martinml>; APPROVED <18 MAR 2003 by izenbei0>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: CONSULTATIVE GROUP MEETING FOR THE PHILIPPINES DECEMBER 9 AND 10
TAGS: EAID, EFIN, RP, IBRD
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005